

## Country Update for 2016

### Background

After decades of instability, towards the end of the 90s Cambodia embarked on a path of economic growth, achieving a significant rise in living standards, albeit from a very low base. A vibrant but fragile development of social and labour market institutions has accompanied this growth but social protection has remained inadequate.

In 2012 the ILO's Social Protection Expenditure Review found the overall Social Protection Floor (SPF) to be incomplete, with few statutory provisions apart from those benefiting public-sector workers. Along with the development of social security provisions in the formal sector, the report highlighted the need to pursue policies and programmes that relieved the plight of the poor and vulnerable.

The adoption of the National Social Protection Strategy for the Poor and Vulnerable (NSPS-PV) 2011-2015 raised expectations for increased government spending in social assistance, as well as improved ownership and coordination of what has been widely regarded as a fragmented and donor-driven system. While this was a strong start, overall, the strategy's mid-term review of 2013 found mixed results. When the strategy expired in 2015, the Government decided to take a different approach.



## The Social Protection Policy Framework 2016 - 2025

The Royal Government's long-term vision for social protection in Cambodia is to build an effective and financially sustainable system which serves as a policy tool to reduce and prevent poverty, vulnerability and inequality, while at the same time boosting human development and national economic growth. The Policy Framework aims at harmonizing, integrating and strengthening existing schemes and expanding the social protection floor to respond to all contingencies throughout the life-cycle. The system envisioned rests on two main pillars: social assistance and social insurance.

The ten year roadmap foresees major legal, institutional and financial reforms to support a gradual expansion of coverage, in line with the country's expanding economy and fiscal space. Beginning with the enhanced governance of the system, the Government will establish a National Social Protection Council to lead the reform. The Council will be composed of members from key line ministries, and will most likely be chaired by the MEF who will in turn also host the Social Protection Technical Secretariat. Its main tasks will include (i) coordinating policy formulation on social protection; (ii) monitoring and evaluating the implementation of policy; and, (iii) ensuring synergy between the two pillars of the system. In terms of operators, the intention is to merge the three existing social security funds into a National Social Insurance Fund that will manage all contributory schemes. A Social Assistance Agency is also being considered.

The draft Policy Framework was approved by a high-level inter-ministerial meeting in November 2016 and is now awaiting approval by the Council of Ministers, expected to review it in early 2017.

## Recent Developments

In June 2015, the Government of Cambodia established a Technical Working Group (TWG) to develop a broader Social Protection Policy Framework, inclusive of social assistance and social insurance. Led by the Ministry of Economy and Finance (MEF), the Framework calls for important reforms across both areas, and prioritizes the rationalization of the contributory system, in particular pensions.

One of the advantages of this new TWG is indeed the fact that different ministries had the chance to work together, including key actors like the MEF who are not always involved in such discussions from the beginning. This opens up a unique window of opportunity for the advancement of the country's SPF.

As a key global actor on social protection, the ILO has provided extensive technical support throughout the process in collaboration with a number of partners. The ILO took the leadership on the pension's reform, but also provided technical advice and inputs to the social health protection and social assistance sections of the framework. One of the ILO's comparative advantages was indeed the broad perspective that this cross-cutting work provided.

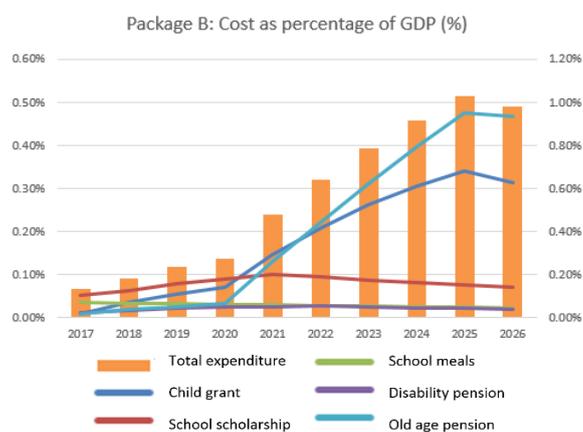
### I. Social assistance for the poor and vulnerable

The goal of establishing a comprehensive and sustainable social assistance system had been tackled by CARD in 2011 through the launch of the NSPS-PV. However, limited progress has been achieved under this strategy in the way of institutionalizing government social assistance programmes. Plans to develop a new phase of the strategy were put on hold as the TWG requested CARD to prepare a Social Assistance Policy Framework (SAPF) to be fed into the larger policy. The ILO has been an active partner in the group coordinated by UNICEF, particularly providing perspective on the relationship between contributory and non-contributory schemes.

Early in the year, CARD and UNICEF requested the ILO to perform a costing of the income-support schemes proposed in the SAPF: a child grant; school scholarships; school meals; and, disability and old age pensions.<sup>1</sup> The ILO report costed a large number of scenarios in order to provide government with evidence on the implications of different choices in terms of coverage and benefit levels. These were presented in four main packages. Overall, it's difficult to judge the affordability of each package without further clarity on the fiscal space available, or of the government and public's will to give priority to these measures over other policy areas. However, it's important to note that the total cost

<sup>1</sup> In collaboration with the GIZ, the ILO has previously prepared a costing for the expansion of Health Equity Funds to vulnerable populations.

## HIGHLIGHTS OF THE REPORT



- Cambodia allocates 10% of its social protection expenditure on social assistance, compared to a 36% average across the region. The macroeconomic context is favourable, with a healthy real GDP growth expanding the fiscal space available. The decreasing poverty trends mean that as coverage of schemes expand, the percentage of GDP required to finance social assistance will be increasingly smaller.
- In terms of social assistance financing the rising old-age dependency ratio is compensated by the decline in youth dependency ratio overtime. However, these trends mean that within the next two decades a shrinking working population will need to support an expanding elderly population, making the case for investment in human capital beyond the poorest.
- The effectiveness of school is limited by their focus on higher school grades as well as low benefit amounts. The modest coverage of the scheme means both challenges could be addressed without significantly increasing overall costs.
- The child grant promises the most return on investment. Assuming a benefit of USD10, cost scenarios range between 0.12% of GDP for a means-tested scheme, to 0.9% of GDP for a universal one. Under any scenario the cost of this scheme gradually decreases over time.
- Under any scenario, the aging population drive the cost of both the disability and old age pensions upwards over time. The scope of both schemes will depend on whether the state approaches social protection as an instrument of insurance against social risks or a narrower safety net for the poor.
- Given the high share of workers in the informal economy, contributory schemes cannot be relied on to provide comprehensive old age protection. A universal social pension providing a flat rate to all people over 60 could cost from 0.51% of GDP to 1.03%, depending on the benefit amount.

of a package is strongly driven by the pace of expansion of the different schemes and thus the government has the possibility to balance its accounts by taking an integrated and coordinated approach towards the implementation of the SAPF over the next decade.

After results were presented in April, the Government decided to prioritize the implementation of a cash grant for pregnant women and children of ages 0-5. In May, with EU-SPS funding, UNICEF and ILO commissioned a joint study to provide insights on the government institutions best placed to take over the newly proposed schemes.<sup>2</sup> The report found that capacity for implementation and coordination is limited at both national and sub-national levels. Most importantly, it found no single institution with both the policy-making mandate and ground presence to operationalize a national social assistance scheme. In response to this vacuum, the TWG is now discussing the possibility of establishing a Social Assistance Agency, although its specific role and functions must still be clarified. Throughout these discussions, the lessons learned through the ILO single window pilot will be key to highlight the need for a more responsive, accessible and integrated system of social assistance benefits, from targeting to grievance processes. The Social Services Delivery Mechanism (SSDM) run from June 2014 to June 2017 under ILO-Korea support.

## II. Social Insurance

As a natural counterpart of the Ministry of Labour and Vocational Training (MoLVT), the ILO has provided technical assistance to the National Social Security Fund (NSSF) since its establishment in 2007. Under the new policy framework, the NSSF is set to take a central role in the expansion of the social protection system with an expanded mandate over contributory schemes for the public and possibly the informal sectors.

### Employment Injury Insurance (EII)

Likewise, the ILO supported the launch of the Employment Injury Insurance in 2008, and has continued to follow-up on the performance of this scheme through periodic actuarial valuations. As of December 2016, the scheme covered more than 1.1 million workers nationwide. The contribution rate has been maintained at 0.80% of total wages and is fully paid by the employer. In 2016 around 20,000 workers benefited from the scheme after work-related accidents through medical care and nursing, temporary and permanent disability benefits, survivors' pensions, caretaker and funeral allowances. The NSSF has now requested the ILO's support to expand coverage of this scheme to the growing construction sector, which will signal the first

entry point for informal workers into statutory social security. The EU-SPS will be financing the ILO to carry out the initial feasibility studies over the next year. As the NSSF expands into other populations and branches it will be key to learn from the lessons learned through the implementation of the EII so far. The ILO plans to carry out an evaluation of the scheme in 2017. This work – which will include a survey with employers and workers – will aim at supporting the NSSF to continuously improve the efficiency and effectiveness of their processes.

This work will be complemented by a close collaboration with another ILO project focusing on the Occupational Health and Safety (OSH) of construction workers, thereby providing a joint approach of prevention and protection.

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### Social Health Insurance

The second branch the NSSF was intended to launch for private sector workers was a Social Health Insurance (SHI). In support of this objective, the ILO and GIZ partnered under the P4H framework to conduct the appropriate actuarial valuations in 2011 and 2014, as well as generally building capacity.

In January 2016, the Prime Minister signed into law the establishment of social health insurance (SHI) for private sector workers; the second scheme for workers covered under the Labour Law. Various related regulations were approved in the following months. The new scheme provides a basic benefit package which includes medical care and hospitalization, prevention services and daily allowances during work absences resulting from sickness, maternity or accidents taking place outside of the workplace.

The scheme is co-financed equally between workers and employers through a contribution of 1.3% of net wages each. Contribution must be at a minimum 2,600 Riels (USD 0.65) and a maximum of 13,000 Riels (USD 3.25) per month. The first phase of expansion is targeting the provinces of Phnom Penh, Kandal and Kompong Speu, where most garment and footwear factories are located. The first contributions were collected in September 2016; by the end of the year, more than 295,000 workers had been registered into the scheme and around 100,000

<sup>2</sup> Pak, Kimchoeun, 2016. Capacity Assessment for the Coordination and Implementation of Social Assistance Programs in Cambodia.

had used it to access health services. Although the scheme is currently available to NSSF members and survivors only, expansion to dependents is foreseen when capacity allows.

Leveraging on this scheme, and in line with the Policy Framework, the NSSF will be launching a second SHI branch for civil servants in 2017, effectively acting as a single payer. At the request of the MEF, with ILO-Korea project financing, the ILO carried out the actuarial review for this scheme which will cover civil servants of the legislative, executive and judiciary branches as well as other public institutions like the police, but not the armed forces. The study presented a financial assessment of the planned scheme and estimated the required contribution rates to provide similar benefits to those of the private sector scheme. If implemented, it will be the first step towards a contributory system for the public sector social security, which has historically been financed directly from the national budget.

### Pensions

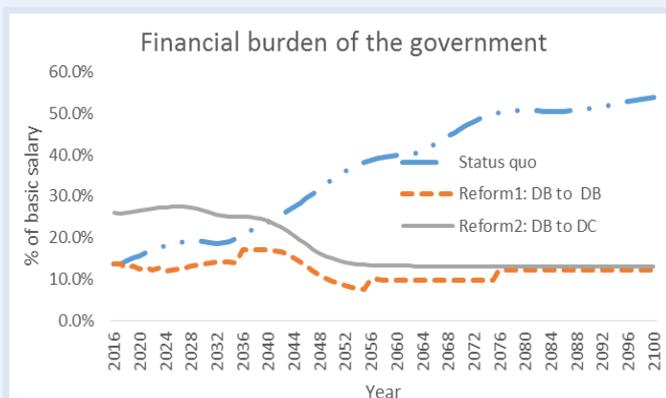
To date, only civil servants have benefited from statutory pensions, leaving the majority of the population vulnerable to old age poverty. Managed under the National Social Security Fund for Civil Servants (NSSF-C), these pensions are financed directly from the national budget without any contribution from employees. A rapidly increasing wage bill has made this into a fiscally unsustainable situation. In this context, an early version of the Policy Framework proposed the establishment of a Defined Contribution (DC) pension system for both the public sector and potentially for the private sector too.

At the request of the MEF and MOLVT, the ILO provided an analysis of this reform proposal from the point of view of population coverage, adequacy of benefits and affordability and financial sustainability.<sup>3</sup> After exploring the different set of reforms available to Cambodia, the report presented the financial implications of the different options through an abbreviated model. The draft Policy Framework calls for a full actuarial review before a final decision is made on the reform. AFD and ILO will be co-financing this full review through a year-long project which provide policy and design options based on the actuarial assessment of coverage, benefit adequacy and financial sustainability. Legal and investment experts will also provide technical advice to pave the way for the reform. Finally, the project includes a strong social dialogue component with regular tripartite consultations as well as capacity building for government, workers and employers. The MOLVT plans to launch the private sector pension under the NSSF by 2018.

<sup>3</sup> ILO. March, 2016. Brief Policy Paper: Policy Considerations and options for a comprehensive pension system in Cambodia.

## Policy options for a comprehensive old age protection system in Cambodia

The Cambodia old age protection system faces two major challenges today. First, since only civil servants are entitled to a pension, just 5% of the elderly receive a pension. It is imperative that the country expands coverage before the demographic aging process accelerates. Second, existing pensions are paid out of the national budget and thus the increasing wage bill is rendering the system financially unsustainable. The establishment of a contributory system for those with capacity to contribute is imperative to ensure its continuation.



Social security pensions can be calculated on the basis of a defined benefit (DB) or defined contribution (DC) plans. There is a big global debate on the merits of DB vs. DC. In the case of Cambodia, the analysis shows that a system grounded on a DC solution (individual saving accounts) would imply an immediate contribution level much higher than needed under a DB scheme, which benefits from the country's demographic returns and expected productivity gains over the next decades. Even if the same contribution rates were set for both models, the replacement rates achieved by a DC plan would be far below those of a DB scheme, meaning that DB delivers more adequate pension amounts. The basic level of development of the Cambodian financial sector reduces the probability that sufficient returns can be generated from individual saving accounts, putting even more pressure on the adequacy of pensions under a DC model. Finally, contrary to the original intention of the reform, the modelling of the civil servant's scheme shows that a transition to DC would significantly increase the burden of the state for several decades to come.

Regardless of the model selected, reaching universal old age coverage will require complementing contributory schemes with a tax-funded social pension.

## Social Protection Code

In order to ensure that the Policy Framework is implemented, the MEF intends to develop a legal framework through a single text that would regulate the entire social protection system. The Social Protection Code would fill the legal gaps for the expansion of the system left by the Social Security Law of 2002.

The ILO and GIZ have partnered to support the Government in this endeavour. Three joint missions took place in 2016 to help establish the expectations of different stakeholders with respect to this legal reform. While a full drafting process will not be possible until the Policy Framework is adopted, preliminary recommendations from national and ILO legal experts include carrying out a regulatory impact assessment to map potential overlaps and vacuums with respect to existing legislation. The public consultations required in the process of developing new legislations are expected to become a forum to validate the vision of the Policy Framework and begin the process of designing the schemes it endorses.

The GIZ and the ILO will continue to partner on this work throughout 2017.

## Recommendations for the way forward in 2017

The year of 2016 was perhaps the most promising for social protection in Cambodia since the launch of the NSSF in 2007. The current reform represents a major window of opportunity to expand Cambodia's social protection floor. The enhancement of synergies between contributory and non-contributory schemes will be essential to establish coherent system and can play an important role in the development of innovative policy solutions.

### *Sustainable Cooperation*

Such an ambitious agenda will require maintaining the high level of coordination that the TWG has brought about. One of the first tasks of the new Social Protection Council will be to ensure that external funding is appropriately channelled to support the government's objectives, as stated in the new Policy Framework. As Cambodia moves steadily towards lower middle income-status, there will be an increased need for Government to raise the aggregate level of public expenditure in social protection. This may include reallocating public expenditure, increasing tax revenues or expanding contributory revenues.

### *Solid Institutions*

The NSSF is being tapped for a major role in the new system but it will be important not to expand its mandate and tasks too widely too fast, so as not to risk the hard-earned gains of the past 10 years. When preparing to manage its new branches, the institution

will benefit most from partners that provide comprehensive institutional support and capacity building, ensuring the integrity of its tripartite structure is not compromised by the reforms. The proposal for a Social Assistance Agency will need to be considered carefully and in the full context of the policy, management and implementation functions involved in a non-contributory social protection system.

### *Strategic Expansion*

There are many development partners willing to support the NSSF to expand coverage of the newly established health insurance branch. The most strategic way to achieve this in the short term will be to assist the NSSF to (i) include dependants into existing schemes for private and public sectors and (ii) expand legal access to persons not covered by the Labour Law, specifically workers in companies with less than 8 workers. In terms of social assistance the needs are large, the government will need to establish clear priorities and commitments for financing.

### *Innovation for the Informal Sector*

As they are rolled out, contributory schemes will need to be adapted to labour market characteristics, particularly to accommodate the large numbers of workers in non-standard forms of work and informal employment. This adaptation calls for innovative policies and new solutions for law and compliance enforcement. Employment injury insurance has long been the first step in the expansion of protection to this sector and is the only nationally implemented scheme in Cambodia. Investing in the extension of this scheme to significant groups in the informal sector could well pave the way for their future access to other branches of the NSSF like health insurance and pensions. Having said this, it is also important to recognize that many will not have the capacity to contribute which is why it's important for social assistance to reach a wider portion of the vulnerable population. The ID Poor will be key in this respect and might require reforms to support an improved system.

## Contact Information

ILO National Coordinator for Cambodia  
Phnom Penh Centre, Building F, 2<sup>nd</sup> Floor  
Corner Sihanouk (274) & Sothearos (3) Blvd.  
Phnom Penh, Cambodia  
Tel.: +855 23 220 817  
Internet: [www.ilo.org/asia](http://www.ilo.org/asia)  
Email: [ramirezlopez@ilo.org](mailto:ramirezlopez@ilo.org)

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